

House Engrossed

State of Arizona
House of Representatives
Forty-sixth Legislature
First Regular Session
2003

CHAPTER 143

HOUSE BILL 2154

AN ACT

AMENDING SECTIONS 20-481.01 AND 20-481.25, ARIZONA REVISED STATUTES; RELATING TO INSURANCE HOLDING COMPANY SYSTEMS.

(TEXT OF BILL BEGINS ON NEXT PAGE)

1 Be it enacted by the Legislature of the State of Arizona:

2 Section 1. Section 20-481.01, Arizona Revised Statutes, is amended to
3 read:

4 20-481.01. Investment limitations; exemptions

5 A. Any domestic insurer, either by itself or in cooperation with one
6 or more persons, may organize or acquire one or more subsidiaries subject to
7 the limitations of this article. Such subsidiaries may conduct any kind of
8 business or businesses and the authority to do so shall not be limited by
9 reason of the fact that such subsidiaries are subsidiaries of a domestic
10 insurer.

11 B. In addition to investments in common stock, preferred stock, debt
12 obligations and other securities permitted under all other sections of this
13 title, a domestic insurer may, pursuant to subsection A of this section:

14 1. Invest in common stock, preferred stock, debt obligations and other
15 securities of one or more subsidiaries in amounts which do not exceed the
16 lesser of ten per cent of such insurer's assets or fifty per cent of such
17 insurer's surplus as regards policyholders, provided that after such
18 investments the insurer's surplus as regards policyholders will be reasonable
19 in relation to the insurer's outstanding liabilities and adequate to its
20 financial needs. In calculating the amount of such investments, INVESTMENTS
21 IN DOMESTIC OR FOREIGN INSURANCE SUBSIDIARIES AND HEALTH CARE SERVICE
22 ORGANIZATIONS SHALL BE EXCLUDED, AND there shall be included total net monies
23 or other consideration expended and obligations assumed in the acquisition
24 or formation of a subsidiary including all organizational expenses and
25 contributions to capital and surplus of such subsidiary whether or not
26 represented by the purchase of capital stock or issuance of other securities,
27 and all amounts expended in acquiring additional common stock, preferred
28 stock, debt obligations, and other securities and all contributions to the
29 capital or surplus, of a subsidiary subsequent to its acquisition or
30 formation.

31 ~~2. With the approval of the director, invest any amount in common~~
32 ~~stock, preferred stock, debt obligations, and other securities of one or more~~
33 ~~subsidiaries, if the insurer's total liabilities, as calculated for national~~
34 ~~association of insurance commissioners annual statement purposes, are less~~
35 ~~than ten per cent of assets, provided that after such investment the~~
36 ~~insurer's surplus as regards policyholders, considering such investment as~~
37 ~~if it were a disallowed asset, will be reasonable in relation to the~~
38 ~~insurer's outstanding liabilities and adequate to its financial needs.~~

39 ~~3.~~ 2. Invest any amount in common stock, preferred stock, debt
40 obligations and other securities of one or more subsidiaries provided that
41 IS ENGAGED OR ORGANIZED TO ENGAGE EXCLUSIVELY IN THE OWNERSHIP AND MANAGEMENT
42 OF ASSETS AUTHORIZED AS INVESTMENTS FOR THE INSURER IF each such subsidiary
43 agrees to limit its investments in any asset so that such investments will
44 not cause the amount of the total investment of the insurer to exceed any of
45 the investment limitations specified in paragraph 1 of this subsection or in

chapter 3, article 2 of this title, applicable to the insurer. For the purpose of this paragraph, "the total investment of the insurer" includes any direct investment by the insurer in an asset and the insurer's proportionate share of the investment in an asset by any subsidiary of the insurer, which shall be calculated by multiplying the amount of the subsidiary's investment by the percentage of the insurer's ownership of such subsidiary.

4. 3. With the approval of the director, invest any amount in common stock, preferred stock, debt obligations or other securities of one or more subsidiaries, provided that after such investment the insurer's surplus as regards policyholders will be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs.

~~5. With the approval of the director, invest any amount in the common stock, preferred stock, debt obligations, or other securities of any subsidiary exclusively engaged in holding title to or holding title to and managing or developing real or personal property, if, after considering as a disallowed asset so much of the investment as is represented by subsidiary assets which if held directly by the insurer would be considered as a disallowed asset, the insurer's surplus as regards policyholders will be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs, and if following such investment all voting securities of such subsidiary would be owned by the insurer.~~

C. Investments in common stock, preferred stock, debt obligations or other securities of subsidiaries made pursuant to subsection B of this section shall not be subject to any of the otherwise applicable restrictions or prohibitions contained in this title applicable to such investment of insurers.

D. Whether any investment pursuant to subsection B of this section meets the applicable requirements is to be determined before the investment is made by calculating the applicable investment limitations as if the investment had already been made, taking into account the then outstanding principal balance on all previous investments in debt obligations, and the value of all previous investments in equity securities as of the date they were made.

E. If an insurer ceases to control a subsidiary, it shall dispose of any investment therein IN THE SUBSIDIARY made pursuant to this section within three years from the time of the cessation of control or within such further times as the director may prescribe, unless at any time after such investment has been made, such investment has met the requirements for investment under any other section of this title, and the insurer has SO notified the director thereof.

F. For purposes of this section, in determining whether an insurer's surplus as regards policyholders is reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs, the following factors shall be considered:

- 1 1. The minimum expendable surplus amount required by section 20-211.
- 2 2. The size of the insurer as measured by its assets, capital and
- 3 surplus, reserves, premium writings, insurance in force and other appropriate
- 4 criteria.
- 5 3. The extent to which the insurer's business is diversified among the
- 6 several lines of insurance.
- 7 4. The number and size of risks insured in each line of business.
- 8 5. The extent of the geographical dispersion of the insurer's insured
- 9 risks.
- 10 6. The nature and extent of the insurer's reinsurance program.
- 11 7. The quality, diversification and liquidity of the insurer's
- 12 investment portfolio.
- 13 8. The recent past and projected future trend in the size of the
- 14 insurer's surplus as regards policyholders.
- 15 9. The surplus as regards policyholders maintained by other comparable
- 16 insurers.
- 17 10. The adequacy of the insurer's reserves.

18 Sec. 2. Section 20-481.25, Arizona Revised Statutes, is amended to
19 read:

20 20-481.25. Acquisitions involving insurers not otherwise
21 covered; anticompetitive considerations; civil
22 penalty; definitions

23 A. Except as provided in subsection B of this section, this section
24 applies to any acquisition in which there is a change in control of an
25 insurer authorized to do business in this state.

26 B. This section does not apply to the following, except as provided
27 under subsections C and D of this section:

28 1. An acquisition otherwise subject to approval or disapproval by the
29 director pursuant to this article.

30 2. A purchase of securities solely for investment purposes as long as
31 the securities are not used by voting or otherwise to cause or attempt to
32 cause the substantial lessening of competition in any insurance market in
33 this state. If a purchase of securities results in a presumption of control
34 under section 20-481, the purchase of securities is not solely for investment
35 purposes unless the director of insurance of the insurer's state of domicile
36 accepts a disclaimer of control or affirmatively finds that control does not
37 exist and the disclaimer action or affirmative finding is communicated by the
38 domiciliary insurance director to the director of insurance of this state.

39 3. The acquisition of a person by another person if both persons are
40 neither directly nor through affiliates primarily engaged in the business of
41 insurance and if preacquisition notification is filed with the director
42 pursuant to subsection C of this section thirty days before the proposed
43 effective date of the acquisition. Preacquisition notification is not
44 required if the acquisition would otherwise be excluded from this section by
45 any other provision of this subsection.

1 4. The acquisition of already affiliated persons.

2 5. If, as an immediate result of an acquisition, the combined market
3 share of the involved insurers in any market would not exceed five per cent
4 of the total market, there would not be an increase in any market share or
5 the combined market share of the involved insurers in any market would not
6 exceed twelve per cent of the total market and the market share increases by
7 more than two per cent of the total market. For the purpose PURPOSES of this
8 paragraph, "market" means direct written insurance premiums in this state for
9 a line of business as contained in the annual statement required to be filed
10 by insurers licensed to do business in this state.

11 6. An acquisition for which a preacquisition notification is required
12 pursuant to this section because of the resulting effect on the ocean marine
13 insurance line of business.

14 7. An acquisition of an insurer whose domiciliary director of
15 insurance finds that the insurer is failing, that there is no feasible
16 alternative to improve the insurer's condition and that the public benefits
17 that would result from improving the insurer's condition through the
18 acquisition exceed the public benefits that would result from not lessening
19 competition and the domiciliary director of insurance communicates these
20 findings to the director of insurance of this state.

21 C. An acquisition under subsection B of this section may be subject
22 to an order pursuant to subsection ~~E~~ F OF THIS SECTION unless the acquiring
23 person files a preacquisition notification and the waiting period has
24 expired. The acquired person may file a preacquisition notification.
25 Information submitted under this subsection is confidential. The
26 preacquisition notification shall be in a form and contain the information
27 that is prescribed by the national association of insurance commissioners
28 relating to those markets which are not exempt from the provisions of this
29 section. The director may require additional material and information that
30 ~~he~~ THE DIRECTOR deems necessary in order to determine if the proposed
31 acquisition, if consummated, would lessen competition or tend to create a
32 monopoly. The information may include an economist's opinion on the
33 competitive impact of the acquisition in this state and a summary of the
34 economist's education and experience that indicates ~~his~~ THE DIRECTOR'S
35 ability to render an informed opinion. The waiting period begins on the date
36 the director receives a preacquisition notification and ends thirty days
37 after the date of receipt or on termination of the waiting period by the
38 director, whichever is earlier. Before the waiting period ends, the director
39 on a one-time basis may require the submission of additional information that
40 is relevant to the proposed acquisition. The waiting period shall end thirty
41 days after the director receives the additional information or terminates the
42 waiting period, whichever is earlier.

43 D. No acquisition subject to the provisions of this section shall
44 substantially lessen competition in any line of insurance in this state or
45 tend to create a monopoly. The director may enter a cease and desist order

under subsection F of this section if there is substantial evidence that the effect of the acquisition may be to substantially lessen competition in any line of insurance in this state or may tend to create a monopoly or if the insurer fails to file adequate information pursuant to subsection C of this section. The director has the burden of showing prima facie evidence of a violation of this subsection. In determining if a proposed acquisition would lessen competition or tend to create a monopoly, the director shall consider the following:

1. An acquisition covered under subsection B of this section that involves two or more insurers competing in the same market is prima facie evidence of a violation of this subsection if:

(a) The market is highly concentrated and the involved insurers possess the following market shares:

| <u>Insurer A</u> | <u>Insurer B</u> |
|------------------------|-----------------------|
| (i) four per cent | four per cent or more |
| (ii) ten per cent | two per cent or more |
| (iii) fifteen per cent | one per cent or more |

(b) The market is not highly concentrated and the involved insurers possess the following market shares:

| <u>Insurer A</u> | <u>Insurer B</u> |
|------------------------|------------------------|
| (i) five per cent | five per cent or more |
| (ii) ten per cent | four per cent or more |
| (iii) fifteen per cent | three per cent or more |
| (iv) nineteen per cent | one per cent or more |

A highly concentrated market is a market in which the share of the four largest insurers is seventy-five per cent or more of the market. Percentages not shown in the tables are interpolated proportionately to the percentages that are shown. If more than two insurers are involved, exceeding the total of the two columns in the table is prima facie evidence of a violation of this subsection. For the purposes of this paragraph, the insurer with the largest market share is deemed to be insurer A.

2. A significant trend toward increased concentration exists if the aggregate market share of any grouping of the largest insurers in the market, from the two largest to the eight largest, has increased by seven per cent or more of the market over a period of time that extends from a base year five to ten years before the acquisition up to the time of the acquisition. Any acquisition or merger under subsection B of this section that involves two or more insurers competing in the same market is prima facie evidence of a violation of this subsection if:

(a) There is a significant trend toward increased concentration in the market.

1 (b) One of the insurers involved is one of the insurers in a grouping
2 of large insurers whose market share has increased by seven per cent or more.

3 (c) Another involved insurer's market is two per cent or more.

4 E. If an acquisition is not prima facie evidence of a violation of
5 subsection D of this section, the director may establish the requisite
6 anticompetitive effect based on other substantial evidence. If an
7 acquisition is prima facie evidence of a violation of subsection D of this
8 section, a party may establish the absence of the requisite anticompetitive
9 effect based on other substantial evidence. Relevant factors in making a
10 determination under this subsection include market shares, volatility of
11 ranking of market leaders, number of competitors, concentration, trend of
12 concentration in the industry and ease of entry into and exit from the
13 market.

14 F. If an acquisition violates this section, the director may enter an
15 order:

16 1. Requiring an involved insurer to cease and desist from doing
17 business in this state with respect to the line or lines of insurance
18 involved in the violation.

19 2. Denying the application of an acquired or acquiring insurer for a
20 license to do business in this state.

21 G. The director shall not enter an order pursuant to subsection F of
22 this section unless a hearing is held and notice of the hearing is issued
23 before the end of the waiting period prescribed in subsection C of this
24 section and not less than fifteen days before the hearing. The hearing shall
25 be concluded and the order shall be issued no later than sixty days after the
26 end of the waiting period. The director shall include with each order a
27 written decision setting forth his THE DIRECTOR'S findings of fact and
28 conclusions of law. The order does not become final earlier than thirty days
29 after it is issued. Before the order becomes final the involved insurer may
30 submit a plan to remedy within a reasonable time the anticompetitive impact
31 of the acquisition. Based on the submitted plan or other information, the
32 director shall specify the conditions, if any, that would remedy the aspects
33 of the acquisition causing the violation and shall vacate or modify the
34 order. An order does not apply if the acquisition is not consummated.

35 H. An order shall not be entered under subsection F of this section
36 if:

37 1. The acquisition will yield substantial economies of scale or
38 economies in resource utilization that cannot be achieved feasibly in any
39 other way and the public benefits that would arise from the economies exceed
40 the public benefits that would arise from not lessening competition.

41 2. The acquisition will increase substantially the availability of
42 insurance and the public benefits of the increase exceed the public benefits
43 that would arise from not lessening competition.

1 I. The director, after notice and a hearing, may impose one or more
2 of the following civil penalties against a person who violates a cease and
3 desist order that is in effect:

4 1. Up to and including ten thousand dollars for every day of
5 violation.

6 2. Suspension or revocation of the person's license.

7 J. An insurer or other person who fails to make a filing required by
8 this section and who fails to demonstrate a good faith effort to comply with
9 the filing requirement is subject to a civil penalty of not more than fifty
10 thousand dollars.

11 K. For THE purposes of this section:

12 1. "Acquisition" means any agreement, arrangement or activity that
13 results in a person acquiring directly or indirectly the control of another
14 person, including the acquisition of voting securities, assets, bulk
15 reinsurance and mergers.

16 2. "Insurer" means a company or group of companies under common
17 management, ownership or control.

18 3. "Involved insurer" means an insurer that acquires or is acquired,
19 is affiliated with an acquirer or acquired or is the result of a merger.

20 4. "Market" means the relevant product and geographical markets. In
21 determining the relevant product and geographical markets, the director shall
22 give due consideration to the definitions or guidelines, if any, adopted by
23 the national association of insurance commissioners and to information, if
24 any, submitted by the parties to the acquisition. In the absence of
25 sufficient information to the contrary, the relevant product market is
26 assumed to be the direct written insurance premium for a line of business
27 that is used in the annual statement required to be filed by insurers doing
28 business in this state. The relevant geographical market is this state.

APPROVED BY THE GOVERNOR MAY 5, 2003.

FILED IN THE OFFICE OF THE SECRETARY OF STATE MAY 5, 2003.

Passed the House February 03, 2003

Passed the Senate April 28, 2003,

by the following vote: 57 Ayes,

by the following vote: 30 Ayes,

0 Nays, 1 Not Voting
2 Vacancies
Jake Flake
Speaker of the House

Norman L. Moore
Chief Clerk of the House

0 Nays, 0 Not Voting
Ken Bennett
President of the Senate

Norma Chastain
Asst. Secretary of the Senate

EXECUTIVE DEPARTMENT OF ARIZONA
OFFICE OF GOVERNOR

This Bill was received by the Governor this

29 day of April, 2003

at 11:00 o'clock A. M.

Pandra Ramirez
Secretary to the Governor

Approved this 5 day of

May, 2003,

at 10³⁰ o'clock A. M.

Jan Brewer
Governor of Arizona

EXECUTIVE DEPARTMENT OF ARIZONA
OFFICE OF SECRETARY OF STATE

This Bill was received by the Secretary of State

this 5 day of May, 2003,

at 3:59 o'clock P. M.

Janice K. Brewer
Secretary of State

H.B. 2154